Guernsey Financial Services Commission

Executive Office

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"Financial stability, macro-prudential policy & mutual regulatory recognition"

Bailiwick Risks 2017

- IMF 2010 Assessment
  - Bailiwick doesn't domestically generate systemic risks
  - Greatest risk to banking system credit/counterparty risk

- 2017 Financial Stability Committee
  - Bailiwick doesn't domestically generate systemic risks
  - Greatest risk to banking system credit/counterparty risk

Global Financial Stability Risks 2017

1. Excessive debt
2. Low interest rate environment
3. Chinese imbalances

Financial Stability, Risk Outlook, GFSC 2016 Annual Report

1. Excessive debt
2. Central bank policy
3. Chinese credit growth

Wolfgang Schäuble, October, 2017

Brexit risks

- Current issues more matter of economic risks rather than financial stability risks
  - Real impact on growth, consumer spending, investment and the capital account
  - Variation of the UK countercyclical buffer in 2016 little more than demand management.
- Real economic risks from a hard Brexit – major financial shock to EU27
  - Requirement for additional €40bn capital for European banks, AFME
  - 85% of all European commercial paper issued in London.
- Real stability risks from a hard Brexit relate to contract uncertainty
  - Allianz has 1m UK policy holders, 9m EU27 policy holders needing insurance contract revision.
  - Mitigated by single brush of legal pen, clause in the exit agreement? Sam Woods, DG, BoE, November 2017.

International standards

Macro prudential policy has effectively two approaches:

1. Making the system more resilient.
2. Preventing problems.

Policy development focuses on the former.

IMF, FSB and BIS, August 2016.

Elements of Effective Macroprudential Policies, suggestions include:

- A clear mandate that forms the basis for assigning responsibility for taking macroprudential policy decisions.
- *A broad range of policy tools to address systemic risk over time and from across the financial system.*

FSB/IOSCO, January 2017.

Policy Recommendations to Address Structural Vulnerabilities from Asset Management:

- 14 recommendations

Financial stability, prudential carveout and protectionism: a Brexit Battleground

Elements of a Model Free Trade Chapter: Canadian Comprehensive Economic Trade Agreement (CETA) provides a potential template:

- Article 13 indicates broad financial services scope but narrowed by 13.7 which refers to more limited scope in annex
- **Includes a fairly open ended ‘prudential’ carve out, Article 13.16**
- Underneath the umbrella of the CETA joint committee, creates a Financial Services Committee which:

  shall meet annually, or as it otherwise decides, and shall:

  (a) supervise the implementation of this Chapter;

  (b) carry out a dialogue on the regulation of the financial services sector with a view to improving mutual knowledge of the Parties' respective regulatory systems and to cooperate in the development of international standards as illustrated by the Understanding on the dialogue on the regulation of the financial services sector contained in Annex 13-C;

- Specific disputes settled by a separate arbitration panel

EU mood music is that banking, clearing and securities candidates for consideration as providing systemic risk issues (EMIR 2.0 June 2017)

Preferred UK financial services approach

‘Mutual recognition – a basis for Market Access after Brexit’

International Regulatory Strategy Group, City UK, March 2017

Broadly, given the conclusion that third country equivalence is asymmetric, somewhat arbitrary and limited in scope in financial services dossiers, the IRSG called for a mutual recognition regime and concludes any agreement requires:

1. Criteria for access
2. Mechanisms for dialogue
3. Dispute resolution model

Supporting Europe’s Economies and Citizens: a modern approach to financial services in an EU-UK Trade Agreement, UK Finance, November 2017

Three principles. A framework for financial services should:

1. be built on mutual recognition;
2. approach cross border contracting issues based on nature of client; and
3. be based on a high degree of regulatory and supervisory co-operation.

Mutual recognition narrative

- Consistently applied global capital standards support global capital market efficiency.
- Global standards include both prudential rules, Basel III, and high level principles of regulation and supervision, Basel Core Principles, IAIS Insurance Core Principles, and IOSCO Principles etc.
- There is support for continuing commonly applied capital standards emerging from banking and insurance groups operating globally and associated representative bodies such as the IIF.
- Concurrently, there is a body of opinion suggesting that global standards including core principles could be used as basis mutual recognition and market access agreement.

Guernsey & mutual regulatory recognition

The purpose

- Exploit our position as stable secure jurisdiction through more effective promotion.
- Press for participation in future FTAs and better UK market access by proactive participation in mutual recognition debate and default technical position as coherent regulatory regime.

The activities

- Direct representation, DfIT papers.
- House of Lords EU Financial Affairs Sub Committee Submission.
- Participation in IRSG regulatory coherence workstream.
- Social media article and forthcoming more proactive media programme.
- Future Legatum report.

Pointers for 2018

- Financial stability concerns: a Trojan horse for protectionism not purely in the Brexit context.

- Mutual regulatory recognition: leverage and positioning work into broader Bailiwick strategies.

- Global financial stability risks remain broadly similar and remain concerning – policy maker actions perhaps single biggest cause of risk in system, Catch 22.